

Washington State

Department of Financial Institutions

SECURITIES DIVISION

Deborah Bortner, Director

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Contact Deborah Bortner: 360-902-8760

Wall Street scams break into Top 10 investment frauds , say securities regulators

OLYMPIA (August 26, 2002) – Deborah Bortner, securities director for Washington, today released a list of the “Top 10” investment scams, frauds, or sales abuses facing state securities regulators in 2002. New to the list this year are unscrupulous brokers, conflicts of interest on Wall Street, charitable gift annuities, and oil and gas scams.

“The bear market has investors on the run,” says Bortner, “and too many of them run straight into the traps set by con artists who pitch their scams as safe alternatives with guaranteed high returns - two things that never match up.” She says investors concerned about low interest rates on fixed investments and volatility in the stock market are desperate enough to believe anything and try anything.

The 2002 list was again topped by independent insurance agents selling risky or fraudulent securities. Bortner says that although most independent insurance agents are honest, too many are letting high commissions lure them into selling high risk or fraudulent investments.

The Top 10 investment scams, ranked roughly in order of prevalence or seriousness, include: **Unlicensed individuals, such as independent insurance agents, selling securities.** In hundreds of cases nationwide, high commissions are luring insurance agents into selling investments they know little about, promising high returns with little or no risk. “Insurance agents selling viaticals, prime bank notes, and promissory notes are by far our biggest enforcement problem,” says Bortner. To verify that a person is licensed to sell securities, she urges consumers to call the state Securities Division in Olympia.

New on the list at number two is unscrupulous stockbrokers. The declining stock market has caused some brokers to cut corners or resort to outright fraud, Bortner says. In addition, some investors have grown more cautious and are scrutinizing their brokerage statements for unexplained fees, unauthorized trades or other irregularities. Stockbrokers selling investors unsuitable investments is a common complaint here in Washington, she adds.

Another new category at number three is analyst research conflicts. After the New York Attorney General’s office investigated Merrill Lynch, they entered into a settlement agreement on charges that the firm issued misleading research reports leading to buy

recommendations in order to win investment banking business. State investigators are now reviewing materials provided by a dozen firms for possible securities law violations.

Promissory notes made their regular appearance on the list, this time at number four. These are often sold by independent insurance agents and issued by little-known or non-existent companies promising high returns – upwards of 15 percent monthly – with little or no risk.

Prime bank scams promise investors triple-digit returns through access to the investment portfolios of the world's elite banks. Based on an ongoing state Securities Division investigation of an alleged prime bank scheme, a U.S. District Court in Dallas, Texas last March enjoined a Tacoma firm, Resource Development International (RDI) and its two principals, David and James Edwards, and froze their assets. The Edwards, along with RDI and two other firms, are thought to have bilked more than 1,300 investors nationwide of nearly \$100 million in a prime bank scheme that targeted retirement funds. Investors were promised annual returns of 48 to 120 percent with complete safety of principal, and with 50 percent of excess profits going to humanitarian causes, according to Bortner.

Viatical settlements came in sixth on the list. Originated as a way to help the gravely ill pay their bills, these interests in the death benefits of terminally ill patients are always risky and sometimes fraudulent. Last year, the Securities Division found that two corporations and six insurance agents had sold more than \$1 million in unregistered viatical investments to at least 45 Washington residents. "This was one of a series of cases involving insurance agents who aren't licensed to sell securities selling investment products not registered in our state," says Bortner. "Before selling a viatical investment in Washington state, insurance agents should check with us to see if it needs to be registered. They must also be licensed to sell securities before trying to sell viaticals or any other investments."

Affinity fraud. Many scammers use their victim's religious or ethnic identity to gain their trust – knowing that it's human nature to trust people who are like you – and then steal their life savings. From "gifting" programs at some churches to foreign exchange scams targeted at Asian Americans, no group seems to be without con artists who seek to take advantage of the trust of others. The main problem in these cases is that investors let their guard down and don't seek out the information they need to make an informed investment decision.

Charitable gift annuities. These annuities are transfers of cash or property to a charitable organization. The value of the annuity is less than the value of the cash or property, with the difference constituting a charitable donation. While most annuities offered by charitable organizations are legitimate investments, investors should be cautious of little-known organizations or those that provide only sketchy information.

Oil and gas scams rise in frequency with predictions of oil shortages or a rise in gas prices, just as has happened this year.

Equipment leasing. While many equipment leasing deals are legitimate, Bortner says thousands of investors have been scammed by individuals selling interests in payphones, ATMs or Internet kiosks. "Earlier this year," she says, "at least 100 Washington citizens were sold nearly \$4 million in unregistered securities in the form of pay telephones or telephone equipment and service agreements. "We were able to stop several other similar schemes before they got a real foothold in Washington," Bortner says. She encourages state residents considering a business or work-at-home opportunity to "check them out before writing a check."

Washington's Securities Division may be contacted by calling 1-800-372-8303 (toll free in-state) or you can visit them on the Web at <http://www.dfi.wa.gov/>. Investors can also find out if the person offering the investment is licensed to sell securities in the State of Washington and whether they have any disciplinary history.

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